Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matters of High Cost Universal Support	)	WC Docket No. 05-337
Universal Service Contribution Methodology	)	WC Docket No. 06-122
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45

REPLY COMMENTS OF THE MINNESOTA INDEPENDENT COALITION

The Minnesota Independent Coalition ("MIC")[1] submits the following Reply Comments in response to the Public Notice[2] issued by Federal Communications Commission ("Commission") seeking comments on requests for clarification and guidance filed by the Universal Service Administrative Company ("USAC").[3] USAC's requests concern several policy issues related to the universal service high-cost support mechanism and contribution methodology.

The MIC supports the comments filed by a number of entities and organizations in their recommendations on three specific topics:

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[1] The MIC is an unincorporated association of over seventy-five small, Incumbent Local Exchange Carriers ("ILECs") providing local exchange service to primarily rural areas in Minnesota. MIC members are responsible for providing telecommunications service to customers throughout 50% of Minnesota's land mass, including service to over 250 small communities and their surrounding rural areas. MIC members average approximately 4,800 access lines, although half of the MIC members have fewer than 1,800 access lines. The average number of access lines per MIC member exchange is approximately 1,100 with half serving fewer than 600 access lines.

[2] Public Notice, *Comment Sought on Request for Universal Service Fund Policy Guidance Requested by the Universal Service Administrative Company*, WC Docket No 05-337, WC Docket No. 06-122, CC Docket No. 96-45, DA 09-2117, released September 28, 2009.

[3] Letter from Richard A. Belden, Chief Operating Officer, USAC, to Julie Veach, Acting Chief, Wireline Competition Bureau, Federal Communications Commission, WC Docket No. 05-337 (filed August 19, 2009) (*USAC August 19, 2009 Letter*); Letter from Richard A. Belden, Chief Operating Officer, USAC, to Julie Veach, Acting Chief, Wireline Competition Bureau, Federal Communications Commission, WC Docket Nos. 05-337; 06-122 (filed August 21, 2009) ("*USAC August 21, 2009 Letter*").

- Eligible telecommunications carriers ("ETCs") should not be required to individually list each of the supported services enumerated in 47 C.F.R. §54.101 in order to comply with the advertising requirement stated in 47 C.F.R. §54.201;

- The Commission's document retention rule applicable to High-Cost support recipients, 47 C.F.R. §54.202(e), should not be retroactively applied to periods prior to the effective date of that Rule; and

- Income taxes attributable to the shareholders of Subchapter S corporations are properly included in a carrier's revenue requirement and are recoverable through Universal Service support.

The MIC joins with the filing entities and organizations to request action by the Commission to clarify its position on these three topics, as outlined above and discussed below.

1. ETCs should not be required to separately list each supported service when advertising the availability of and charges for such services.

The MIC joins with many commentors to request that ETCs should not be required to separately list each of the supported services enumerated in Section 54.101 of the Commission's rules and their corresponding charges in advertisements.[4] This position is supported both by the language of the controlling statute and rules, and by common sense.

As USTA notes, the wording of Section 54.201(d)(2) of the Commission's rules echoes the words of 47 U.S.C. §214(e)(1)(B) and requires ETCs to "advertise the availability of such services and charges therefore."[5] The statute and regulation do not require the advertisement of "each" of the services enumerated in Rule 54.101(a)(1-9). Congress could have used the words

[4] Comments of the United States Telecom Association ("USTA"), October 28, 2009, pp. 2-3; Comments of the Nebraska Rural Independent Companies ("Nebraska Companies"), pp. 3-5; Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies and the Western Telecommunications Alliance ("OPASTCO/WTA"), pp. 8-9; Comments of the Independent Telephone & Telecommunications Alliance ("ITTA"), pp. 10-11; Comments of the National Telecommunications Cooperative Association ("NTCA"), pp. 4-6.
[5] USTA at 2-3.

"each service" in place of "such services," if it intended to hold ETCs to a point-by-point listing of each of the supported services in advertisements.[6]

The MIC agrees with the ITTA that a requirement to advertise the availability and charge for each of specific supported services is inconsistent with 47 C.F.R. §54.405(b), which requires carriers to advertise Lifeline services "in a manner designed to reach those likely to qualify for service."[7] Many of the commentors observe that consumers simply do not understand what are each of the individual service components listed in Rule 54.101(a)(1-9),[8] and, in any event, these components are not customarily offered for sale on an individual basis. Rather, they are provided under the umbrella of "local telephone service."[9]

MIC concurs that advertising the availability and price for each of the supported services is not reasonable and would confuse consumers with too much detail.[10] As NTCA observes, the message of availability and pricing for the supported services is conveyed to consumers far more effectively when described as "local telephone service" rather than by listing component parts.[11] Individual listing of the supported services would be similar and as ineffective, as NTCA explained, to requiring automobile dealers to list separately the price of the tires, steering wheel, antenna and seats when advertising a car for sale; the consumer cares about the total price and functionality of the car and not its individual parts.[12]

ETCs reasonably concluded that advertising each of the supported services individually was not required by the controlling statute or rules. USAC's request for Commission

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[6] *Id.*
[7] ITTA at 11.
[8] OPASTCO/WTA at 8.
[9] Nebraska Companies at 3-4; USTA at 3; OPASTCO at 8.
[10] NTCA at 5.
[11] *Id.*
[12] NTCA at 5.

clarification of its Rule 54.201(d)(2) demonstrates that the Rule's requirements are unclear, and it would therefore be inappropriate to initiate recovery action against ETCs for their reasonable interpretation of an ambiguous rule.[13] However, if the Commission determines that ETCs' advertisements must separately identify and provide pricing for each of the supported services listed in Rule 54.101(a), the MIC joins with other commentors in requesting that such a requirement should only apply on a going-forward basis.[14]

2. The High-Cost Program Document Retention Rule should not apply retroactively.

The MIC agrees with commentors that it would be improper and contrary to established law to retroactively apply the Commission's High Cost Program document retention rule[15] (the "Document Retention Rule") to periods prior to its effective date.

Between 1986 and the 2008 adoption of the Document Retention Rule, carriers were provided flexibility to develop their own record retention schedules,[16] but the Commission reserved the right "to prescribe specific retention period" for records that are needed but not found "not to be generally available. "[17] The Commission's adoption of the Document Retention Rule is an exercise of this reserved power, requiring recipients of High Cost Program funds to retain certain records for a period of five (5) years from the date of disbursement.

The Document Retention Rule established, for the first time, document retention rules specifically applicable to High-Cost support recipients.[18] Its purpose is abundantly clear: "[t]he

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[13] OPASTCO at 9.
[14] OPASTCO at 9; NTCA at 5-6.
[15] 47 C.F.R. § 54.202(e).
[16] NECA at 7-8.
[17] NECA at 8, quoting *Revision of Part 42, Preservation of Records of Communication Common Carriers*, CC Docket No. 84-283, Report and Order, 1986 WL 290829 at para. 32 (F.C.C) (August 22, 1986).
[18] OPASTCO/WTA at 4.

Commission promulgated this requirement because the absence of a record retention rule until that time impeded USAC and USF auditors from evaluating Program compliance."[19] However, as many of the commentors note, it is only fair (and possible) to evaluate Program compliance based upon rules in effect during time periods being audited and not on wholly-new requirements not in place for those periods.[20]

The MIC agrees with several of the commentors that the general prohibition against retroactive rulemaking, under the Administrative Procedures Act and interpretive case law, should be followed by the Commission to apply the Document Retention Rule only on a prospective basis.[21] As both the ITTA and NECA comments describe, it is well-settled that retroactive rulemaking is permitted only where there is express authorization for that application.[22] There is no such authorization for retroactive application of the Document Retention Rule. Therefore, there should be no retroactive application of the Document Retention Rule, and the Commission should clearly state that no remedial action should be initiated against carriers that did not maintain documentation for periods prior to the effective date of the Document Retention Rule.

3. Income taxes attributable to S-Corporation shareholders should continue to be recoverable through USF Support.

The MIC joins with other commentors to encourage validation of the historical industry practice of allowing income taxes attributable to S-corporation shareholders to be included in a carrier's revenue requirement and recoverable through USF.[23] The MIC agrees that state and

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[19] Comments of TDS Telecommunications Corp. ("TDS") at 2.
[20] OPASTCO/WTA at 4; TDS at 5; NPCA at 6; USTA at 3-4; ITTA at 3, 7-8.
[21] ITTA at 4-8; Nebraska Companies at 6-7; NECA at 8-9.
[22] ITTA at 5; NECA at 8.
[23] NECA at 5-7; Nebraska Companies at 7-8; USTA at 5; OPASTCO/WTA at 9-12; NTCA at 2-4.

federal income taxes are an expense that rural ILECs incur as part of providing communications services to their customers. As a result, the federal income tax expense that arises from such service should be recoverable regardless of corporate form of the ILEC.[24] As the commentors observe, such a result is consistent with a prior Commission ruling with respect to S-corporation cable television companies[25] and with the ratemaking practices of another federal regulatory agency.[26]

As NECA describes in its comments, this issue has already been addressed by the Commission in relation to S-corporation cable television companies.[27] In that proceeding, the Commission recognized that cable operators "operate under diverse ownership forms including corporations, Subchapter S corporations, partnerships (including partnerships of other ownership forms) and sole proprietorships."[28] The Commission recognized that "[r]egulators have generally permitted rate-regulated companies to recover income taxes in order to compensate the utility for taxes imposed directly on the utility" and ruled to "design an income tax treatment that permits recovery of income taxes regardless of the form of ownership of the regulated cable services enterprise."[29] Similar treatment is warranted with respect to telecommunications carriers.

USAC, as well as NECA and OPASTCO/WTA, also explain that permitting S-corporation carriers to recover income tax expense would be consistent with a policy statement

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[24] OPASTCO/WTA at 9.
[25] NECA at 5-6; OPASTCO/WTA at 10.
[26] NECA at 6-7; OPASTCO/WTA at 11.
[27] NECA at 5, citing to *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service*, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd. 4527 (1994).
[28] *Id.* at para. 138.
[29] NECA at 6.

on income tax allowances issued by the Federal Energy Regulatory Commission ("FERC").[30] FERC explained:

> While the pass-through entity does not itself pay income taxes, the owners of a pass-through entity pay income taxes on the utility income generated by the assets they own via the device of the pass-through entity. Therefore, the taxes paid by the owners of the pass-through entity are just as much a cost of acquiring and operating the assets of that entity as if the utility assets were owned by a corporation.[31]

The MIC encourages the Commission to follow the reasoning and precedent of its prior ruling on the tax treatment of cable operators and FERC's policy statement, to validate the current standard industry practice of allowing appropriate shareholder income tax to be imputed when determining an S-corporation or other "pass through" entity's interstate revenue requirement. The MIC further requests that the Commission instruct its auditors that, for the purposes of Universal Service support, income taxes attributable to S-corporation activities are recoverable through Universal Service support.

While recovery of High Cost program support could be significant if S-corporation carriers are not permitted to impute shareholder income tax in determining a carrier's interstate revenue requirement,[32] the MIC agrees with the Nebraska Companies that the most likely outcome of such a decision would be conversion of S-corporations to C-corporations, with much less impact on the High Cost program than might otherwise result.[33]

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[30] *USAC August 21, 2009 Letter* at 4; NECA at 6; OPASTCO/WTA at 11.
[31] NECA at 7.
[32] *USAC August 21, 2009 Letter* at 5.
[33] Nebraska Companies at 8.

Conclusion

The MIC requests that the Commission act to clarify its Rules and address the issues presented by USAC, in order to facilitate compliance with USF rules and regulations. Specifically, the MIC urges the Commission to rule that:

(1) Compliance with Section 54.201(d) requires only the advertising of local exchange service, and no retroactive remedial action shall be taken against ETCs which offered all of the supported services but advertised only local exchange telephone service;

(2) Section 54.202(e) is to be given prospective effect only, and there should be no remedial action taken against carriers that did not maintain documentation for periods prior to the establishment of the High-Cost Document Retention Rule; and

(3) Consistent with current industry practice, a carrier electing S-Corporation status may impute the income taxes paid by the shareholders that arise from providing telephone services for the purpose of determining the carrier's revenue requirement, and direct USF auditors to recognize such income taxes.

Date November 12, 2009

Respectfully submitted,

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and

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Attorneys on Behalf of the Minnesota Independent Coalition

CERTIFICATE OF SERVICE

I, Karen E. Berg, hereby certify that a copy of the Reply Comments of the Minnesota Independent Coalition was sent via electronic mail, on this day, the 12th day of November, 2009, to those listed below:

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